

Brazil

In 2012 Brazil's economy grew modestly, by around 1.2%, reflecting uncertainty stemming from the international crisis and its impacts on the country's production sectors and investment, especially in manufacturing. Employment and real wages also continued to rise, although at lower rates than in 2011, and unemployment remained low. Inflation held steady at around 5.5%, within the central bank's target range.

On the economy policy front, a number of processes set in motion in 2011 were consolidated, including the reduction of the reference interest rate, the Special System of Clearance and Custody (SELIC), which came down to 7.25% in 2012. The currency depreciation begun in 2011 accumulated a 30% decline, from 1.6 reais to the United States dollar in July 2011 to 2.09 in November 2012. At the same time, the authorities deployed an active fiscal policy to stimulate short-term demand and promote structural change.

Consumption was again the most dynamic demand component, thanks to good labour market conditions, continued growth in lending and lower interest rates. Investment was somewhat weaker, with public investment spending and demand for new loans from the National Bank for Economic and Social Development (BNDES) both rising more slowly than in 2011. In addition, national capital goods production was down by 11.8% in January-October 2012 with respect to the prior-year period and capital goods imports rose just 2.6% in that period.

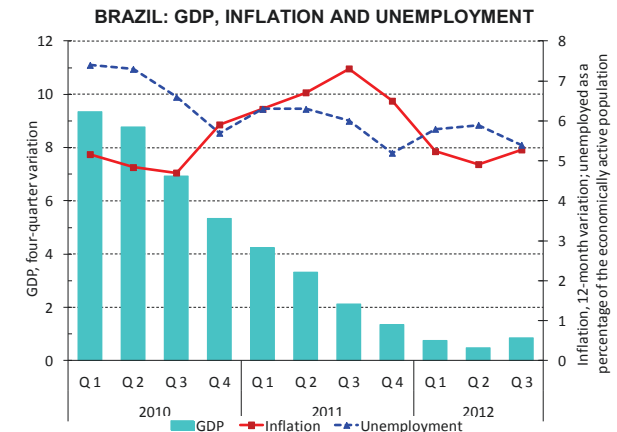
Growth is projected to border 4% in 2013, on the strength of an upturn in manufacturing, still buoyant domestic demand and increased exports, given the competitiveness gains made through the growth stimulus of currency depreciation.

In 2012, Brazil's economic policy consisted of a steady adjustment to the international crisis and efforts to support growth. The gradual decline in the interest rate begun in August 2011, when the base rate stood at 12%, steered the course of monetary policy. The central bank continued cutting the rate until October 2012, taking it close to 2% in real terms, the lowest level since 2003. The cuts were also aided by changes

to the interest rate set for savings deposits, which used to guarantee real annual yields of almost 6%. Alongside these interest rate developments, the monetary base expanded by 8.9% between October 2011 and October 2012, under pressure from the growth in international reserves and cash in circulation (8.1%).

Lending growth dropped back from 19% in 2011 to 10.2% in the 12 months to September 2012, as banks, fearing a deterioration in the credit portfolio, became more selective. Growth in personal lending slowed from 16.3% to 8.0%, and in business lending from 16.9% to 9.1%. Although the arrears rate was stable at 3.8% in the system overall, in private national banks it rose throughout 2012, from 4.8% to 5.2%.

Fiscal policy was directed towards implementation of growth-stimulus measures through changes to the tax regime or the orientation of spending. In the tax domain, similarly to cuts made in



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

2008 and 2010, temporary reductions were extended in sales tax on automobiles, trucks, cellular telephones, household appliances and construction materials. This was in addition to the decision to shift social security contributions from a payroll basis to a percentage of corporate sales, to lower business costs. Tax hikes and spending were also used to support new investments in industry, especially in innovation. The slower rate of economic growth took a toll on tax receipts, however: the take began to decline in real terms starting in June 2012, and grew by only 0.7% in January-October in real terms. With regard to public spending, social security payments were up by 13% in January-October 2012 over the prior-year period, owing to the rise of almost 8% in real minimum wages. Spending on other social benefits rose too: unemployment insurance by 13.8% and social assistance, including the Bolsa Familia scheme, by 18.4%. In June 2012 the payment of conditional benefits was extended to families with children up to age 6, which is expected to bring the indigence rate in the target population from 13% down to around 5%. Payroll expenditures rose 3.3% in January-October, and a nominal annual pay rise of 5% for the next three years was agreed for federal public servants. Federal government investment rose 23.3% in the first 10 months of 2012 over the year-earlier period, as a result of a subsidized housing scheme called “Minha Casa, Minha Vida”.

With income growth more sluggish and the direct or tax spending measures deployed to support economic growth and social protection, the government acknowledged that it would not be able to meet its primary surplus target of 139 billion reais (3.1% of GDP), without using the mechanisms provided under the law on budget guidelines which allow expenditures to be discounted as investment. It was announced that 25.6 billion of spending would be accounted as investment in order to meet the fiscal target. For the public sector overall, including subnational governments and State-owned enterprises, the central bank calculated a primary surplus of 2.4% of GDP to October, well below the 3.5% registered in the same period of 2011. The smaller primary surplus had only a small impact on the nominal deficit, however, which remained at close to 2.5% of GDP, owing to the fall in interest payments from 5.8% of GDP in 2011 to 4.9% in January-October 2012.

Exchange-rate policy during the year was directed towards consolidating a higher exchange rate of around 2.00 reais to the dollar. The currency depreciated gradually alongside the fall in the base rate

BRAZIL: MAIN ECONOMIC INDICATORS

	2010	2011	2012 ^a
Annual growth rates			
Gross domestic product	7.5	2.7	1.2
Per capita gross domestic product	6.6	1.8	0.4
Consumer prices	5.9	6.5	5.5 ^b
Real average wage ^c	2.1	2.4	3.6
Money (M1)	17.3	6.2	4.3 ^d
Real effective exchange rate ^e	-13.4	-4.7	11.7 ^d
Terms of trade	16.0	7.9	-4.5
Annual average percentages			
Open urban unemployment rate	6.7	6.0	5.5
Central government overall balance / GDP	-1.7	-2.6	-2.2
Monetary policy rate	9.9	11.8	8.8 ^f
Nominal lending rate ^g	38.5	40.7	33.5 ^f
Millions of dollars			
Exports of goods and services	233 515	294 250	284 373
Imports of goods and services	244 202	302 395	305 071
Current account balance	-47 272	-52 481	-54 087
Capital and financial balance ^h	96 373	111 118	76 451
Overall balance	49 101	58 637	22 364

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

^a Estimates.

^b Twelve-month variation to October 2012.

^c Private-sector workers covered by social and labour legislation.

^d Year-on-year average variation, January to October.

^e A negative rate indicates an appreciation of the currency in real terms.

^f January-October average.

^g Preset lending rates for legal persons.

^h Includes errors and omissions.

since August 2011, when the exchange rate stood at around 1.55 reais to the dollar. By the end of 2011, the rate was approaching 1.87 reais=US\$ 1 and by May 2012, it had reached 2.00 reais=US\$ 1. Between May and November 2012, the dollar exchange rate fluctuated between 2.00 and 2.09 reais, with central bank intervention throughout this period. For the most part, this consisted of dollar purchases by the central bank, leading to net accumulation of US\$ 24.4 billion in international reserves between August 2011 and October 2012 and taking the reserve stock to US\$ 377.8 billion.

Lower output growth in 2012 mainly reflects the poor performance of Brazilian industry. In the first 10 months of the year, industrial production was down by 2.9% compared to the prior-year period. This downturn was mirrored across all subsectors, especially in the production of capital goods (-11.8%) and consumer durables (-4.3%). Automobile production was down by 3.3%, despite a number of demand-side incentives. This reflected stock adjustment after strong growth in 2010, as well as slacker growth in consumer credit and the ongoing uncertainty about the impact of the international crisis on the economy. The outlook for the sector is expected to be brighter in 2013, however, as the government maintains and expands fiscal and credit mechanisms,

competitiveness and exports begin to benefit from the currency depreciation, and domestic demand picks up.

In this low-growth environment, the mining sector showed only a small uptick of 0.7% to September 2012, contrasting sharply with the strong expansion driven by the commodity boom in previous years. Construction growth similarly slowed in 2012, to 2.2%. With respect to the agricultural sector, the grain harvest is expected to be up by 1.5%, at 162.6 million tons.

The year-on-year inflation rate fell to 5.45% in October 2012, as against 6.5% a year earlier. A steeper fall in inflation was prevented by a fresh upturn in prices for agricultural products and food services, which rose by 10.4% in the 12 months to October 2012. Domestic fuel price stability and lower prices for automobiles thanks to tax breaks also eased upward pressure on inflation. The employment rate continued to rise in 2012, albeit more slowly. Up to October, net formal employment creation stood at 1.3 million jobs, compared to 1.9 million in the same period of 2011. The sluggish performance of industry and construction held down employment expansion in those sectors, whereas hiring continued in commerce and services.

In October 2012 the unemployment rate stood at 5.3%—an annual average of under 6% for the first time ever. Real average income was 4.8% up on the figure for October 2011 and the real wage bill rose by 8.1% in this period.

Brazil's external accounts in 2012 reflect the impact of the international crisis and of lower domestic growth. As of October, the goods trade surplus was 32.2% lower, at US\$ 17.3 billion, with exports of US\$ 202.3 billion (down 5.5% year-on-year) and imports of US\$ 185.0 billion (down 1.9%). The decrease in exports encompassed both volume and price: the export index fell by a cumulative 4.0% to September for prices and by 1.5% for volume. Volumes were down for all the main product categories by October: commodities by 7.3%, intermediate goods by 9.2%,

and manufactures by 2%. In terms of the main destinations for Brazil's exports, only those to the United States showed growth (9.6%), while those to the Southern Common Market (MERCOSUR) fell by 13.6%, those to the European Union by 8.5% and those to China by 6.1%.

On the import side, prices rose (0.5%) and volumes fell (3.3%). The downturn in imports was concentrated in fuels (-6.8%) and consumer durables (-5.4%). Capital goods imports climbed 2.6%. China consolidated its position as the leading source of Brazilian imports, with a growth rate of 5.2% and a share of 15.5%.

In this period, the deficit on the services account widened to US\$ 33.5 billion (US\$ 31.5 billion in the year-earlier period), still under pressure from net spending on foreign travel, which rose to US\$ 12.9 billion. On the income account, net profit remittances were down (to US\$ 17.7 billion, versus US\$ 29.2 billion in the prior-year period).

As a result, the current account gap was similar to that of 2011 (2.2% of GDP), and the balance of payments was in surplus by US\$ 23.4 billion, around half of the US\$ 53.9 billion surplus registered in 2011.

Direct investment was again the main source of financing, with net inflows of US\$ 56.9 billion, slightly less than the US\$ 59.9 billion recorded in the same period of 2011. In turn, reflecting the uncertain international economy, tax regulations imposed on certain types of capital inflows and the currency depreciation process, portfolio investment inflows fell from US\$ 16.6 billion in 2011 to US\$ 12.2 billion in 2012. Brazil's external assets showed a reversal in 2012 with a net outflow of US\$ 6.4 billion, compared to a net inflow of US\$ 14.3 billion in 2011.

Brazil's external debt, including intercompany loans, stood at US\$ 308.5 billion in October 2012 (US\$ 298 billion in 2011). The combination of this slight rise and the country's growing international reserves have kept the debt-to-GDP ratio at -4%.